

**MULTILATERAL TRADE
NEGOTIATIONS
THE URUGUAY ROUND**

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Negotiating Group on Subsidies
and Countervailing Measures

ELEMENTS OF THE FRAMEWORK FOR NEGOTIATIONS

Communication from the Republic of Korea

Recognizing that the negotiation framework agreed by the TNC is, as stated in its preamble, a flexible guideline to conduct negotiations in a balanced way with a view to improving GATT disciplines relating to all subsidies and countervailing measures, the Republic of Korea formally submits the following proposal dealing with certain elements in the framework. Since there may be other elements which are not covered by this proposal, Korea reserves the right to submit additional proposals at a later date.

With respect to agricultural subsidies, Korea believes that all matters concerning agriculture should be handled primarily by the Negotiating Group on Agriculture; therefore, at this stage, our proposal does not address issues relating to agriculture.

I. Prohibited subsidies

1. Identification

There has been at least an implicit consensus in the negotiating group that certain types of subsidies should be prohibited, depending on their distortive effects on international trade. The use of these subsidies could be readily construed as a violation of multilateral rules; thus, their harmfulness should be clearly evident and their scope should be restrictively regulated.

In this regard, domestic subsidies should not be treated as "prohibited". Their purpose is, as inferred from their designation, the achievement of important domestic objectives of socio-economic policy rather than the artificial intervention to international trade. From this viewpoint, it is apparent that there is no prima facie distortion to trade in the case of domestic subsidies.

The starting point for negotiating how to assign subsidies into this group would be the present illustrative list of export subsidies in the GATT Subsidies Code. However, if the nature of the list remains illustrative like the present case, while acknowledging the need for some special countermeasures in the case where prohibitions are violated,

certainly it would bring forth considerable uncertainties in international trade by unilaterally expanding the scope of prohibited subsidies through arbitrary interpretations.

Therefore, if some kinds of subsidies should be prohibited and on the remedy side exceptional countermeasures should be sanctioned, the present illustrative list should be converted into a definitive and exhaustive one. In addition, any amendment of the list should be made through a multilateral mechanism.

2. Remedies

Remedies for another party's failure to carry out its obligations with regard to the prohibited subsidies can be applied along one of the following two different tracks; problem-solving by application of (i) countervailing duties or (ii) GATT dispute settlement procedure.

- compensatory duties (increased duties without injury test or duties on other products which are exported by the subsidizing country but irrelevant to subsidies granted) should not be permitted.
- in case of adverse effects in third country markets or in the home market of the subsidizing country, remedies could be sought through a multilateral framework of the dispute settlement procedure which is expected to be improved as a result of the Uruguay Round.

The principle of differential and preferential treatment for developing countries should be kept in mind in applying the rules regarding subsidies in this category. Developing countries should be given an adjustment period to reduce or phase out present subsidies which may fall into this category through the negotiation.

II. Non-prohibited but countervailable subsidies

1. Conditions for countervailability

There is a vast area of potentially actionable subsidies which are classified neither as prohibited subsidies nor as apparently non-actionable subsidies. Of subsidies in this "grey" area, only those which meet all the following conditions should be countervailable.

(a) Financial contribution by a government

Financial contribution by a government means expenditures by a government or foregone revenues to a government. However, foregone revenues should not include those occurring under any direct tax or import charge system which allows producers access to raw materials used in the production of export goods at "world prices" and enables them to sell their products at "world prices" in world markets.

If there is no financial contribution by a government, not subsidy can exist. Transactions between the private sector should not be construed as subsidies which GATT intends to discipline.

(b) Sector specificity

A subsidy should be sector specific to be countervailable. The existence of neutral eligibility criteria in applying for a subsidy programme across industries would be sufficient counter-evidence to specificity.

(c) Adverse effects on trade

As the last condition for countervailability, a subsidy should have adverse effects on international trade, causing injury to domestic industry within the meaning of Article VI of GATT. Furthermore, there should be a causal link between the subsidized imports and the injury. In this regard, the application of an injury test should be the sine qua none condition for the application of countervailable duties. If there are no adverse effects, subsidies should be recognized as an important instrument for the promotion of socio-economic policy objectives. In particular, due attention should be given to the following points:

- exclusion of countervailing action for subsidies that are de minimis
- introduction of a minimum market threshold level
- new procedures for a new entrant

If a subsidy is found de minimis, it can be assumed that no material injury exists. A de minimis subsidy may be defined as one whose amount is below X per cent of export value. In the same manner, a countervailing duty should not be imposed on imports whose market share is below X per cent in the importing country.

Unfortunately, there is a tendency to impose countervailing duties on exports from a new entrant without investigation as required under Article VI of GATT, utilizing countervailing duties as if they were ordinary import duties imposed on all imports from a specific country. This requires corrective measures. Without a new investigation, the automatic expansion of outstanding countervailing duties to exports from new entrants should be prohibited.

2. Remedies

A typical remedy for these kinds of subsidies is a countervailing duty. The present Subsidies Code grants investigating authorities wide discretion on initiating and conducting countervailing duty investigations, deciding the existence of material injury or threat thereof, and reviewing countervailing measures. From this excessive discretionary authority, procedural protectionism and/or abuses began to sprout and are flourishing everywhere, which require appropriate corrective actions.

To achieve better discipline on countervailing duty exercises, the mandatory consultation stipulated in Article 3 of the Subsidies Code in order to clarify the factual situation and arrive at a mutually agreed solution should become a prerequisite procedure. Along the same line, any affirmative findings and follow-up countermeasures without a reasonable opportunity for consultation should be regarded as a violation of the Code.

In relation to the standing of a petitioner, serious divergence of practices between signatories has caused unreasonable initiations of the investigation. The practice of one signatory, by which even one firm can appeal the petition, seems to be, without doubt, "unjust" in considering the meaning of the word "major" of Article 6:5 of the Code. There should be clarification on the concept of "on behalf of the industry affected" in terms of the word "major"; hence amendment to the Code in this regard.

On the other hand, the volume of subsidized imports or economic factors used in injury finding could change at any time in a dynamic trade environment. It would be more rational to impose countervailing measures for some fixed period, for example three years, so as not to cause unjustifiable long-term disadvantage to the petitioned party.

The concept of countervailing only the difference between the subsidy on imports and the subsidy on domestic production of the like product is noteworthy. This new approach will certainly help to prevent abuses of countervailing duties which are now widespread.

Furthermore, to prevent unjustified petitions for countervailing duties and relieve administrative burdens of investigating authorities as well as undue harassment to petitioned parties, a provision should be established that, in case of negative findings, all legal expenses or at least more than half paid by the petitioned party in preparing the case shall be borne by the petitioner.

In case of nullification or impairment of the other country's benefits in the home market of subsidizing country or in a third country market, remedies should be taken, in principle, through a multilateral dispute settlement mechanism. Since there is no prima facie relationship between the subsidization level of domestic subsidies and the magnitude of their trade effects, any attempt to establish in advance a certain maximum level of subsidization, by which a countervailable subsidy could be assumed to cause nullification or impairment, should be strongly discouraged.

III Non-countervailable, non-actionable subsidies

i. Conditions for non-counteravailability

There is a group of subsidies which are used not only as corrective measures for market failures but also as basic instruments of government activities for desirable socio-economic objectives. Since governmental activities falling into this category constitute fundamental functions of government, they cannot be viewed as unfair trade practices. They may be classified as follows:

- structural adjustment assistance

Various activities by government for the purpose of retraining labour forces, downsizing an industry, facilitating the readjustment of economic sectors, and compensating the unemployed may belong to this category.

In this regard, special consideration should be given to developing countries. Generally, in developing countries, both developed sectors and less-developed sectors exist at the same time.

Therefore, government support for strengthening any structural vulnerability in less-developed sectors and increasing investment into these sectors should be regarded as "justifiable" and non-actionable.

- expenditures for establishing social overhead capital

One of the basic functions of a government is to supply social overhead capital such as harbour facilities, electric power, or transportation systems etc. These kinds of activities by government or governmental assistance for establishing such social infrastructure should not be regarded as subsidies to be disciplined.

- research and development

Where there exist neutral eligibility criteria to ensure participation in a R and D programme, where there is no restriction to access the knowledge produced through R and D activities, or where results from the R and D can be licensed by foreign firms on the same basis as domestic firms at a reasonable cost, no subsidy would exist.

- regional assistance

Where government aid is designed only to compensate for the dislocation disadvantages of establishing industries in the less developed regions, there is, by definition, no benefit to the recipient at all; hence non-actionable.

- assistance for preventing environmental pollution

This kind of assistance should not be considered as subsidies which GATT intends to regulate within the context of harmful effects on international trade.

- generally available subsidies other than those listed above

These subsidies do not give specific enterprises or industries any particular benefit or advantage not available to other enterprises or industries.

They would include tax incentives applied uniformly on a national basis, general assistance for small and medium-sized enterprises across all industries, general training programmes for workers, etc.

It would be helpful to make an illustrative list of non-actionable subsidies for easy identification of this category. The list should be "illustrative" since, otherwise, basic financial activities by government to achieve policy objectives not listed might be countervailed.

2. Special safeguard

A special safeguard procedure is necessary to prevent non-actionable subsidies from being countervailed by another signatory.

Countervailing non-actionable subsidies in an illustrative list should be presumed to be a violation of GATT obligation. Participants could negotiate the establishment of proper measures to be taken in case of such a violation.

Appendix A - Quantitative Criteria

For the categorization of subsidies, a participant has insisted on the introduction of quantitative criteria as an optimal solution.

However, quantitative criteria not only have such inherent flaws that they could not be workable, but also would ultimately undermine the categorization system of subsidies provided under the current framework for negotiations.

- The application of quantitative criteria introduces asymmetric treatment for subsidies in different categories.

A prohibited subsidy is always prohibited, whether its amount is de minimis or not. On the other hand, a non-actionable subsidy, regardless of its nature or objective, can be countervailable (or even prohibited) at any time whenever certain quantitative parameters are satisfied. Hence asymmetric treatment.

- Quantitative parameters such as subsidy rate and import rate have been suggested.

However, the subsidy rate does not have any prima facie relationship with the trade distortion and the import rate can be determined only ex post. Namely, it is not predictable at the time of introducing a specific subsidy programme. Rather, the import rate is dependent upon general market conditions, as well as, the marketing strategy of the exporter.

- Upon adopted quantitative criteria for subsidy classification, there is no further need to make a distinction between countervailable and non-actionable subsidies.

Under these two categories, subsidies, however detailed and carefully categorized are reduced, once applying quantitative criteria, into only two forms as shown in document MTN.GNG/NG10/W/26;

- (a) de minimis subsidies; therefore non-actionable
- (b) subsidies other than de minimis; therefore always actionable (or prohibited)

Appendix B - Notification

Even though a full and thorough notification is essential in understanding other parties' subsidy programmes, the notification itself is merely one of many GATT obligations.

Notification does not, and should not, change the categorization of a subsidy. Basically, the problem of classifying subsidies should be irrelevant to the notification obligation; therefore, non-actionable subsidies in Section III shall not be automatically presumed to belong to the actionable category in Section II, even in the case where no prior notification is made.